EXECUTIVE BOARD'S ASSESSMENT

At its meetings on 9 September and 23 September 2015, the Executive Board discussed the monetary policy stance. The starting point for the discussion was the analysis published in the June 2015 *Monetary Policy Report*. The Executive Board decided in June to reduce the key policy rate by 0.25 percentage point to 1%. The analysis in the *Report* implied a key policy rate of slightly higher than ¾% in the coming year, followed by a gradual rise. With this path for the key policy rate, there were prospects that inflation would remain slightly below 2.5% in the beginning of the projection period and thereafter hover around 2 percent in the coming years. Capacity utilisation was projected to decline in the coming period, but to move up to a more normal level towards the end of the projection period.

Growth in the world economy remains moderate. There are prospects that growth among Norway's trading partners will gain some momentum ahead, but to a lesser extent than assumed earlier. The uncertainty surrounding developments in China and other emerging economies has heightened. Consumer price inflation is very low among most trading partners, but core inflation is higher. The broad decline in commodity prices through summer will contribute to keeping inflation low. Policy rates are still close to zero in many countries. Market expectations indicate that the expected rise in interest rates among trading partners will occur later and more gradually than expected earlier. Foreign long-term interest rates have also declined since June. In addition to keeping policy rates at a low level, a number of central banks are buying bonds with a view to stimulating economic growth and pushing up inflation.

Oil prices have fallen through summer and have recently hovered somewhat below USD 50 per barrel. The oil price decline reflects increased oil inventories and continued excess supply. At the same time, a further slowdown in emerging economies may push down growth in oil demand. Futures prices reflect expectations of some increase in oil prices, but to a lesser extent than implied by futures prices in June.

The krone has depreciated markedly since June and is weaker than projected in the June *Report*. The depreciation must be seen in connection with the oil price decline and a narrowing of the interest rate differential against other countries.

Growth in the Norwegian economy has so far been broadly in line with the projection in the June *Report*. In August, Norges Bank's regional network contacts reported continued weak output growth. The oil price decline through summer may contribute to a longer period of low growth in the Norwegian economy than projected earlier. Oil investment will likely fall to a further extent than projected in June and lower demand for goods and services in the petroleum industry will reduce activity in the oil service industry. This has spillover effects on the wider mainland economy and may contribute to keeping down wage growth in the years ahead. Lower wage growth may push down demand for goods and services, but will also improve the profitability and competitiveness of Norwegian enterprises. A weaker krone also boosts the profitability of export and import-competing firms.

As expected, unemployment has edged up. While registered unemployment has increased in line with the projections in the June *Report*, LFS unemployment has risen to a further extent. Unemployment has increased in regions closely linked to the oil industry, while it has so far remained stable in other regions. The restructuring in the Norwegian economy brought on by the oil price decline will likely lead to somewhat higher unemployment ahead.

Consumer price inflation adjusted for tax changes and excluding energy products (CPI-ATE) is close to 3%. Prices for both domestically produced goods and services and imported consumer goods have risen at a faster pace than projected in June. The krone has depreciated substantially over a longer period and the exchange rate pass-through appears to be stronger than expected. The krone depreciation since the June *Report* will likely lift inflation further in the coming period.

House price inflation has varied through summer, with wide regional dispersion. Overall house price inflation has been somewhat higher than projected in June. Household debt is still rising somewhat faster than income. Since the reduction in the key policy rate in June, banks have reduced their lending rates slightly more than assumed in the June *Report*.

The Executive Board notes that the analyses in this *Report* show a weaker growth outlook for the Norwegian economy than in the June *Report*. Low wage growth is keeping down cost growth, and inflation is expected to edge down as the effects of the krone depreciation unwind. The analyses imply a reduction in the key policy rate to just above ½% in 2016. Towards the end of the projection period the key policy rate is projected to increase to close to 1%. With this path for the key policy rate, the analyses suggest that inflation will remain close to 3% in the near term, before drifting down to around 2% towards the end of the projection period. The krone exchange rate is projected to appreciate somewhat, but remain weaker throughout the projection period than previously projected. Capacity utilisation in the mainland economy is expected to continue to fall in the period to the end of 2016, followed by some increase partly owing to low interest rates and improved competitiveness.

In its discussion of monetary policy, the Executive Board gave weight to the fact that the oil price decline will curb growth in the Norwegian economy ahead. A weaker krone lifts inflation in the short term. Inflation prospects are lower further out. Combined with the aim of sustaining capacity utilisation, this implies a lower key policy rate. On the other hand, even lower interest rates may fuel property price inflation and debt growth. An overall assessment of the economic outlook and the balance of risks led the Executive Board to conclude that the key policy rate should now be reduced.

At its meeting on 23 September, the Executive Board decided to lower the key policy rate by 0.25 percentage point to 0.75%. The Executive Board's current assessment of the outlook for the Norwegian economy suggests that the key policy rate may be reduced further in the coming year.

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